D. H. Baldwin Company Annual Report 1972

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Financial Highlights

D. H. Baldwin Company and Subsidiaries

(in thousands of dollars except per share amounts)	1972	1971	% of Increase (Decrease)
Financial Services:			
Revenues	**$ 91,573**	$ 80,667	13.5
Assets	**819,218**	665,364	23.1
Income*	**12,445**	9,007	38.2
Manufacturing and Merchandising:			
Net sales and revenues	**63,743**	52,752	20.8
Assets	**33,275**	32,901	1.1
Income*	**839**	1,195	(30.0)
Combined Operations:			
Total revenues and sales	**155,316**	133,419	16.4
Total assets	**852,493**	698,265	22.1
Net income	**9,806**	7,047	39.2
Net income per common share**	**3.44**	2.40	43.3
Cash dividends on common stock	**1,535**	1,426	7.6
Cash dividends per common share**	**.58**	.56	4.0
Market price of common stock**	**23 - 43**	14 - 26	

*Before deduction of unallocated holding company interest and administration expenses.
**Adjusted for stock dividends and stock split.

Officers

Lucien Wulsin
Chairman of the Board

Morley P. Thompson
President

R. S. Harrison
Vice President & Treasurer

Max G. Brooks
Vice President

James E. Carpenter
Vice President

John F. Jordan
Vice President

James M. E. Mixter
Vice President

Eugene Wulsin
Vice President

R. F. Coghill
Secretary

Timothy P. Hartman
Controller

James E. Schwab
Assistant Treasurer

Donald E. Waggoner
Assistant Secretary

Directors

Gordon Adamson
Vice President
Baldwin Piano & Organ Company

Max G. Brooks
Chairman of the Board
The Central Bank and Trust Company
Denver, Colorado

Fred Gretsch, Jr.
Chairman of the Board
The Lincoln Savings Bank
Brooklyn, New York

William M. Hickey
President
The United Corporation
New York, New York

John F. Jordan
Vice President

Lawrence H. Kyte
Partner, Law Firm of
Kyte, Conlan, Wulsin & Vogeler
Cincinnati, Ohio

William A. Mitchell
Retired Chairman of the Board
The Central Trust Company
Cincinnati, Ohio

James M. E. Mixter
Vice President

A. J. Schoenberger
Retired Senior Vice President

Morley P. Thompson
President

Eugene Wulsin
President
The Baldwin Piano Company
(Canada) Limited

Lucien Wulsin
Chairman of the Board

Robert E. Fanning
Director Emeritus

Philip Wyman
Director Emeritus

Letter to Shareholders

Earnings Growth

The year past we continued our growth in earnings, in sales, in revenues, and in assets. Our net earnings per share were $3.44 as compared with $2.40 in 1971, a 43% increase. Our combined net earnings after provision for taxes showed a net increase over 1971 of 39%. They were $9,806,000 as compared with $7,047,000 for the year 1971. This overall increase in earnings consists of the following results:

Financial services income before holding company interest and administration was $12,445,000 in 1972 as compared with $9,007,000 in 1971.

Manufacturing and Merchandising income before holding company interest and administration was $839,000 in 1972 as compared with $1,195,000 in 1971.

Holding company expenses, net of taxes, were $3,478,000 in 1972 as compared with $3,155,000 in 1971.

You will note that our annual Statement of Consolidated Income as well as our Consolidated Balance Sheet has been substantially changed in form from last year. We feel that this change will reflect more accurately our position as a company whose principal activity lies in the area of Financial Services. With this form of a report our Music and Electronic activities are consolidated into Manufacturing and Merchandising operations. Much of our new format is self explanatory with the assistance of the Notes to Financial Statements.

Revenues up 13%

The total revenues of the company showed a substantial increase over 1971. The figures are as follows: $92,412,000 for 1972, $81,861,000 in 1971.

Our Banking and Other Financial Services revenues increased by 14%; our Savings and Loan revenues increased by 20%; and the revenues of the insurance company in which we have a financial interest also showed a significant increase. Details of these increases are found elsewhere in this report.

In our music business we also showed significant increases both in sales dollars and in units sold. Our sales increased by 23% and the value of our products manufactured showed a significant increase over the prior years. During the year we encountered substantial difficulties in increasing our production. During the latter half of the year when the significant volume of business is done in this industry, we were production limited. In addition, we have had during the year a substantial increase in the cost of materials that go into our products. Because of price controls, we have been unable to pass these increased costs on to the consumers of our product. Under Phase II of the Wage and Price Controls, we were a major controlled company during 1972 and did make refunds at the end of the year to a number of our customers. Our inability to meet our production schedules and our inability to pass along increases in costs of materials and labor have contributed to unsatisfactory earnings in our music instrument business.

Lucien Wulsin, Chairman of the Board
D. H. Baldwin Company (left)
Morley P. Thompson, President
D. H. Baldwin Company

Our electronic sales in 1972 showed a small decline over 1971. Inadequate sales in Quantrol Electronics and in Electronic Engineering Systems, Inc. continue to drain profits. In Baldwin Electronics, lack of delivery by our suppliers has held back our sales of hybrid circuits and the slow growth of our sales of alarm systems has contributed to the lack of profitability of our electronics business. Our encoder business continues a steady growth.

Assets

Our past practice has not included a comment on the Assets and Liabilities we manage; they are stated in the consolidated balance sheet. However, we should bring to your attention what has happened in the past five years. Our total Assets have increased 85% from $454,474,000 in 1968 to $841,487,000 in 1972. Our Liabilities have increased from $424,965,000 to $778,303,000.

Proposed Bank Acquisitions

During 1972, we announced our plan to acquire 10 additional banks all located in the State of Colorado. These plans are obviously subject to the approval of the shareholders of these 10 banks as well as our own shareholders and more particularly of the Federal Reserve Board. We are proceeding to submit applications to the Federal Reserve Board for approval of these acquisitions. We expect action on these proposals to be effective during 1973, and will submit these matters for your approval at a special meeting to be held in the second half of 1973 upon completion of the necessary regulatory steps.

Baldwin, a Bank Holding Company

The position of Baldwin as a bank holding company with "grandfather" activities of a non-financial nature, is as of this writing still under review by the Federal Reserve Board. Under the provisions of the 1956 Amendments to the Bank Holding Company Act, the Federal Reserve Board has the obligation to determine which non-banking activities of Baldwin are permissible and which must be terminated or changed to come within the scope of permitted activity. Of those activities engaged in prior to June 30, 1968 it is clear that within this decade we will dispose of our non-musical electronic activities. The Federal Reserve Board has all of our activities under review. We will keep you informed of further developments as they unfold.

Future

It is difficult to predict the continuation of Phase III of the Wage and Price Control and its effect upon the company. It is obvious that we must be able to pass on the effects of wage and price increases if we are to remain effective in the musical instrument business. It is equally difficult to predict the total effect of the dollar devaluation on our competitive position in the music business. We have taken and are taking active steps to put our electronics business on a profitable basis. Our operations in Colorado continue to prosper, and we look forward to continuing growth in this area during 1973. We intend to continue to deploy our assets into those permitted activities where we can show a profitable return to our shareholders. Our proposals to expand our activity in the field of financial services in Colorado should result in increased earnings to our shareholders. We look forward to an improvement in all divisions of our corporate activities during the year 1973.

Respectfully,

Lucien Wulsin

Chairman
March 13, 1973

Financial Services

Baldwin began to expand its financial services in June, 1968 with the acquisition of Central Bank, Denver, Colorado. Since then, while the Company's music and electronics profits have been static, consolidated net earnings have grown from $3,742,000 in 1968 to $9,806,000 in 1972. Net income has increased every year. Financial services have made this record possible. Last year 94% of income before holding company interest and administration was derived from banking, consumer installment lending, savings and loan and insurance activities.

Management intends to enlarge its commitment to financial services. You have already read about plans to add 10 Colorado banks in the Chairman's letter and there are a number of other fields open to bank holding companies such as leasing, mortgage banking and consumer lending. Investing in financial services does not require a large fixed assets base. Labor content is low. On most assets there is a monthly return of principal which can be reinvested in new opportunities.

Baldwin's investment in Financial Services continued to yield excellent returns in 1972. Income, before holding company expenses, as a percentage of net assets invested in banking, savings and loan, and insurance services was 13%, 18%, 16% respectively. Each of these increased from the 1971 figures.

The three Colorado-based companies did well in 1972. Central Bank's income was 30% higher than 1971 largely due to higher earnings in credit card financing and installment lending. Total assets grew by 26% and deposits by 27%. Central ranks 28th among U.S. commercial banks in mortgage servicing, and is the largest installment lender in the 10th Federal Reserve District.

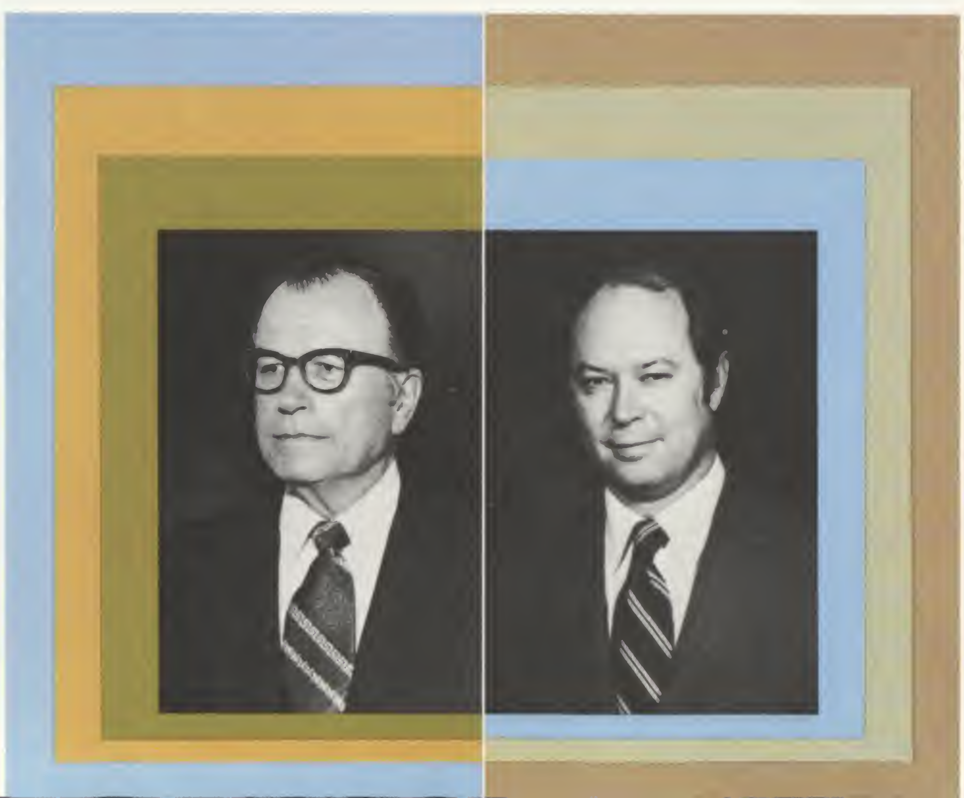
In February, 1973 Central moved into a new bank building, Park Central. It contains a unique "Action Banking Center" which enables the customer to transact all of his banking business in one location. The new building will permit Central to expand and to compete aggressively for new business in the years ahead.

Empire Savings was again able to capitalize on Colorado's construction and home building boom. Income increased 31%, loans, 24% and deposits, 24%. The Association improved its national position and now ranks 115th with assets of $305 million.

During the year, Empire closed 2,200 acquisition, development, construction and permanent mortgage loans, totalling $89 million, 38% higher than 1971. Still, delinquencies were low and real estate owned as a result of foreclosure is negligible. Average yield on the loan portfolio increased throughout the year.

Empire will concentrate on internal growth. Three new branch operations, raising the total to 15, will be opened by mid-year enabling Empire to penetrate new markets. E.S.L. Corp., a wholly-owned service corporation, is involved in real estate developments which will provide a source of loan volume.

Baldwin's investment in National Farmers Union insurance earned $2,525,000 in 1972. This is a 75% increase over the earnings of $1,446,000 in 1970, the year NFU joined the Financial Services group.



Max G. Brooks, Chairman of the Board
The Central Bank and Trust Company (left)
James E. Carpenter, President
The Empire Savings, Building and Loan Association

National Farmers Union sells life and casualty insurance to rural Americans in twenty mid-American states.

The earnings gain was primarily the result of growth in investment income and a casualty underwriting profit. Life and casualty premiums each increased about 11%, adding new funds to the investment portfolio. The casualty company had an underwriting profit of $936,000.

The life company benefited from favorable mortality and accident and health experience. NFU has been emphasizing life insurance sales during the last two years. In that period, first year paid premium on life insurance has grown by 45% and 32% respectively.

While most of last year's growth came from the existing sales force, NFU management is developing additional salespeople for new markets it hopes to enter this year.

Late in the year, Baldwin organized Baldwin Finance Company, a wholly owned installment financing subsidiary. Existing piano and organ retail installment contracts were transferred to the new company along with $6,000,000 of equity capital. This subsidiary provides a vehicle to expand the keyboard installment finance operation. Home improvement financing, which had been a part of Baldwin's installment activity, was discontinued.

Central Bank & Trust Statistical Summary (000)

	1968	1969	1970	1971	**1972**
Assets	$243,835	$261,096	$277,589	$314,405	**$396,593**
Loans, Net	149,834	158,965	165,495	190,473	**226,287**
Deposits	216,616	209,624	236,963	261,571	**331,543**

Empire Savings, Building & Loan Statistical Summary (000)

	1968	1969	1970	1971	**1972**
Assets	$143,620	$180,817	$209,981	$249,126	**$305,262**
Loans	127,249	160,630	187,964	225,750	**279,433**
Deposits	114,277	137,202	149,668	188,147	**234,137**

National Farmers Union Insurances Statistical Summary (000)

	1970	1971	**1972**
Assets	$ 48,820	$ 61,515	**$ 68,977**
Life & Health Premiums	8,350	9,771	**10,824**
Property & Casualty Premiums	18,603	21,884	**24,187**
Investment Income, Net	2,716	3,347	**4,393**

The Living Wall is an environmental display six feet high and ninety feet wide specially commissioned by the Central Bank of Denver. It is positioned just behind and above the teller line in the new Park Central Bank Building.

The Living Wall, the first permanent installation of its kind, is a salute to the people and state of Colorado. It reflects the variety of living patterns and scenic wonders in the Colorado and Denver regions. Scenes range from city skylines to the Maroon Bells as illustrated here.

A computer controls the Living Wall and its 1440 rear projected photographic images which continually appear and fade into other images. The Living Wall and program was designed and created by Communication Arts, Boulder, Colorado.

Manufacturing and Merchandising

The Baldwin mosaic mural in the Cincinnati Union Terminal is the work of German-born Winold Reis, and was photographed recently by Gregory Thorp of Vermont. It is one of fifteen industrial panels selected, forty years ago, for the concourse of the terminal, the last major train station built in America. Currently, nation-wide efforts are being made to "save the terminal", and to preserve the mosaic murals. The concourse and the rotunda — and the murals — have been acclaimed by art historians as prime examples of the Art Deco style in architecture and interior decoration which reached its peak in the twenties and thirties. They symbolize the contemporary need to move forward and grow while at the same time holding on to and doing honor to past traditions and objects of value.

Keyboard Instruments

Share of Market

The music industry enjoyed one of its best years in 1972. Organ unit sales increased approximately 24% and pianos, 14%.

Baldwin's piano and organ sales followed the trend and grew sharply in 1972. Organ sales increased by 16%, piano sales by 3%. The dollar increase was the largest year to year increase in Baldwin's history. Enthusiastic acceptance of the new spinet organ line and the general increase in consumer spending for durable goods produced the sales growth. Market shares, however, did not change greatly. There was a slight increase in Baldwin's share of the organ market and a slight decrease in its share of the piano market.

Sales Training

The year was one in which Baldwin emphasized dealer development and sales training. In the spring, Baldwin conducted nine regional sales meetings in which professional acting and staging was used to present new products and promotions. Over 1000 music dealers and sales people attended these sessions. These meetings were followed by a new intensive sales training course. Baldwin sales and manufacturing representatives conducted classroom sessions at the factories for more than 200 people. These training programs were met with great enthusiasm and will be increased and expanded in 1973.

New Products

The new line of spinet organs made Baldwin a strong competitor in the popularly priced organ market. Baldwin expects that its restyled 40″ vertical piano models will continue to improve its share of that important segment of the piano market. A substantially redesigned seven foot Baldwin grand piano, the SF-10, created an all time record backlog of orders for this smaller version of the famous nine foot concert grand, the SD-10. Syntha-Sound, Baldwin's unique offering in the field of synthesized electronic music, added new novelty voices to the organ plus an unprecedented array of tonal effects.

James M. E. Mixter, Vice President D. H. Baldwin Company (left)
R. S. Harrison, Vice President & Treasurer D. H. Baldwin Company

Manufacturing

While piano and organ production increased 16% in 1972, production volume did not keep pace with sales demand. An effort to improve margins by producing, instead of buying, instrument cases, put an extra burden on factories trying to meet increased schedules. Substantial progress has been made and management believes it can reduce the large year end order backlog to normal levels by mid-year.

During 1972, we continued to invest in new plant and equipment in the Southern plants. The Juarez, Mexico plant began to produce complete pianos for the first time for shipment to the West Coast market.

A Few Problem Areas

With piano and organ sales setting company records, profit improvement should have been greater. In general, Company-owned retail stores did not achieve profit goals. During the year, several stores moved from downtown locations to suburban centers with the resulting temporary loss of sales volume. Teaching labs and Music Centers have not produced expected results. Finally, production volume fell behind the rapid increase in consumer demand for pianos and organs.

Conclusion

The experience of 1972 — greater sales volume but a continuing struggle for profitability — points the way to 1973's keyboard strategy of increased emphasis on organ sales and the sale of those piano models with higher profit margins, substantial improvement in retail store operations, and improved manufacturing efficiency.

Other Musical Instruments

The Gretsch Division, which manufactures and sells guitars, drums and banjos, was not profitable in 1972. Although sales improved by 20%, the higher volume was still not enough to offset manufacturing losses and sales distribution costs. There was further consolidation and reorganization in 1972. Warehousing facilities were combined and personnel was reduced and shifted in order to reduce costs and to develop greater efficiency. At the same time, the sales organization was strengthened and sales support efforts increased. Sales growth from new products and cost control programs should yield better results in 1973.

Financial Review

Sales and revenues and consolidated net earnings established new highs in 1972. Combined revenues increased by $21,897,000, a gain of 16% of which $10,906,000 was from financial services and $10,991,000 from manufacturing and merchandising. This is the fifth consecutive record year. Growth in earnings per common share has averaged 25% per year over the five year period.

Corporate Reorganization

There were three major changes in the corporate structure during 1972. Long term debt, formerly the obligation of Baldwin-Central, Inc., was assumed by the parent, D. H. Baldwin Company, and two new subsidiaries were formed: Baldwin Piano & Organ Company and Baldwin Finance Company. Baldwin Piano & Organ Company with assets of approximately $24,788,000 and $15,000,000 of stockholders equity manufactures and markets musical instruments. Keyboard installment financing is now the responsibility of Baldwin Finance Company. These companies were capitalized so that they should not require financial support from the parent.

Long Term Debt

D. H. Baldwin Company refinanced existing long and short term debt through the issuance of $24,000,000 of long term debt. The Company placed $12,000,000 of 20 year debt privately with institutional investors and borrowed $12,000,000 for 8 years from commercial banks. The proceeds were used to prepay $22,192,000 of long term debt, the remainder applied to reduce short term debt.

Continuous Dividends

Baldwin paid a dividend of $.60 per common share and thus maintained its record of continuous dividend payments dating back to 1935. Dividends on common and preferred stock totalled $2,445,000 compared to $2,350,000 in 1971. For the second straight year, the Company increased the return to shareholders by declaring a 4% stock dividend which was payable to stockholders of record on January 2, 1973.

Financial Flexibility

Baldwin maintains short term financial flexibility through the sale of commercial paper. The paper has a P-3 prime rating from Moody's Investor's Service, Inc. In addition, Baldwin continues to rely on commercial banks for credit and financial assistance. At December 31, 1972, Baldwin had lines of credit totalling $31,000,000 with 19 commercial banks in the United States.

Financial Statements

Audited reports of the major subsidiaries prepared on a separate company basis as well as copies of the financial statements contained in the Form 10-K Report filed with the Securities and Exchange Commission are available from the Company upon request.

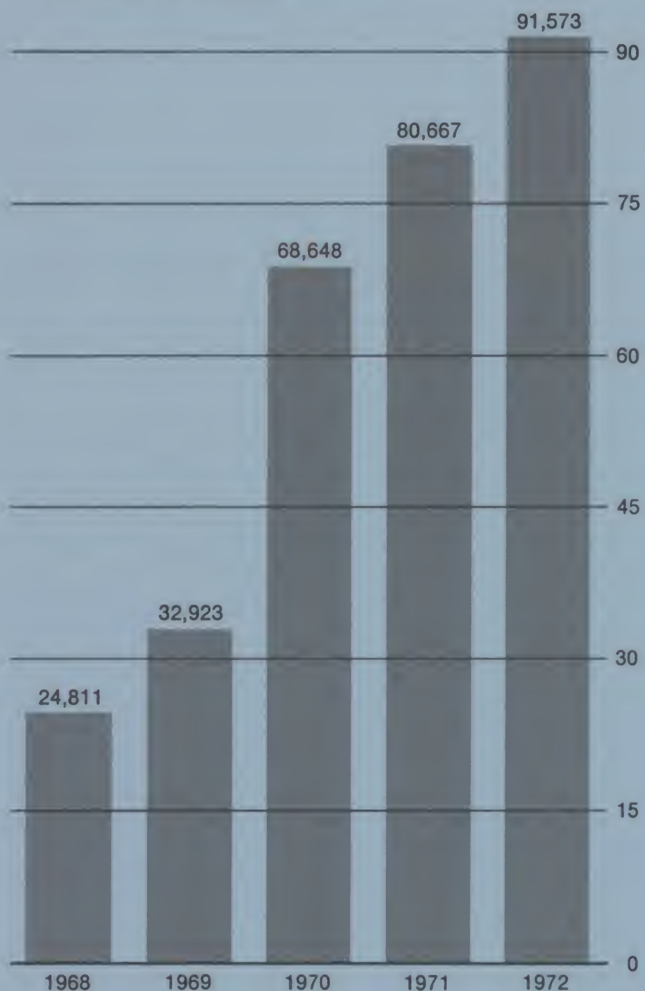
Five Year Comparative Statement

D. H. Baldwin Company and Subsidiaries

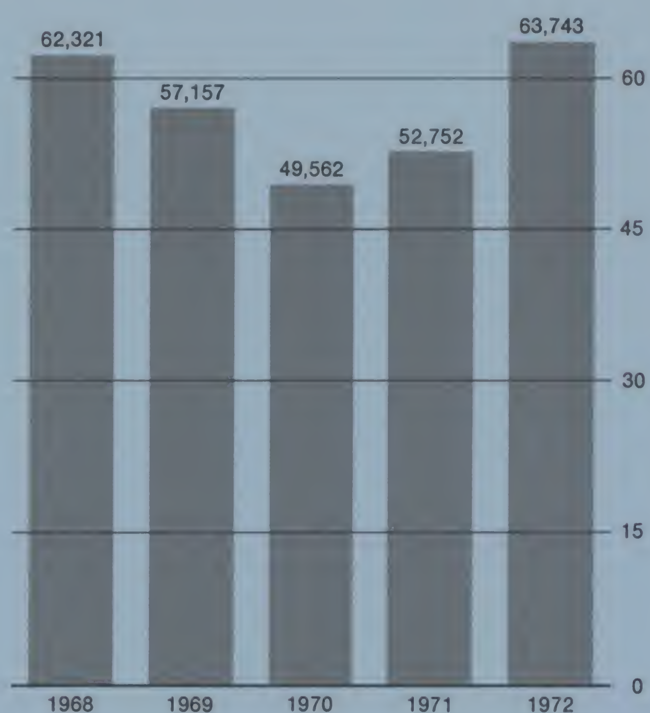
(in thousands of dollars except per share amounts)	1972	1971	1970	1969	1968
Financial Services:					
Revenues	**$ 91,573**	80,667	68,648	32,923	24,811
Assets	**819,218**	665,364	590,251	512,105	436,723
Income*	**12,445**	9,007	7,444	4,560	2,010
Manufacturing and Merchandising:					
Net sales and revenues	**63,743**	52,752	49,562	57,157	62,321
Assets	**33,275**	32,901	31,370	35,063	31,384
Income*	**839**	1,195	778	2,043	2,526
Combined Operations:					
Total revenues and sales	**155,316**	133,419	118,210	90,080	87,132
Total assets	**852,493**	698,265	621,621	547,168	468,107
Net income	**9,806**	7,047	5,024**	4,494	3,742
Net income per common share***	**3.44**	2.40	1.62**	1.79	1.51
Cash dividends on common stock	**1,535**	1,426	1,404	1,396	1,378
Cash dividends per common share***	**.58**	.56	.56	.56	.56
Annual earnings reinvested in the business	**7,361**	4,702	2,694	3,097	2,346
Stockholders' equity	**61,394**	53,283	48,479	45,706	28,048
Book value per common share***	**$ 18.23**	15.32	13.46	12.40	11.17
Average number of common shares outstanding***	**2,588,312**	2,545,131	2,530,459	2,517,342	2,484,439

*Before (net of Federal income taxes) deduction of unallocated holding company interest and administration expenses and 1970 extraordinary credit of $500 for financial services and charge of $421 for manufacturing and merchandising.
**Including net extraordinary credit in 1970 of $79 (equal to .03 per share) net of tax.
***Adjusted for stock dividends and stock split.

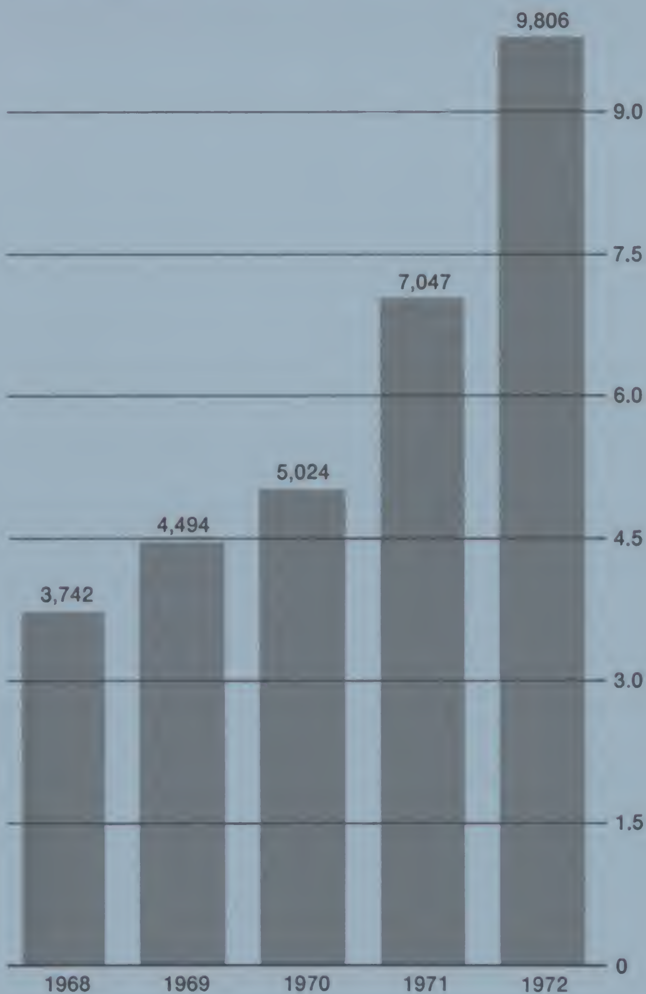
Financial Services: revenues
in thousands of dollars



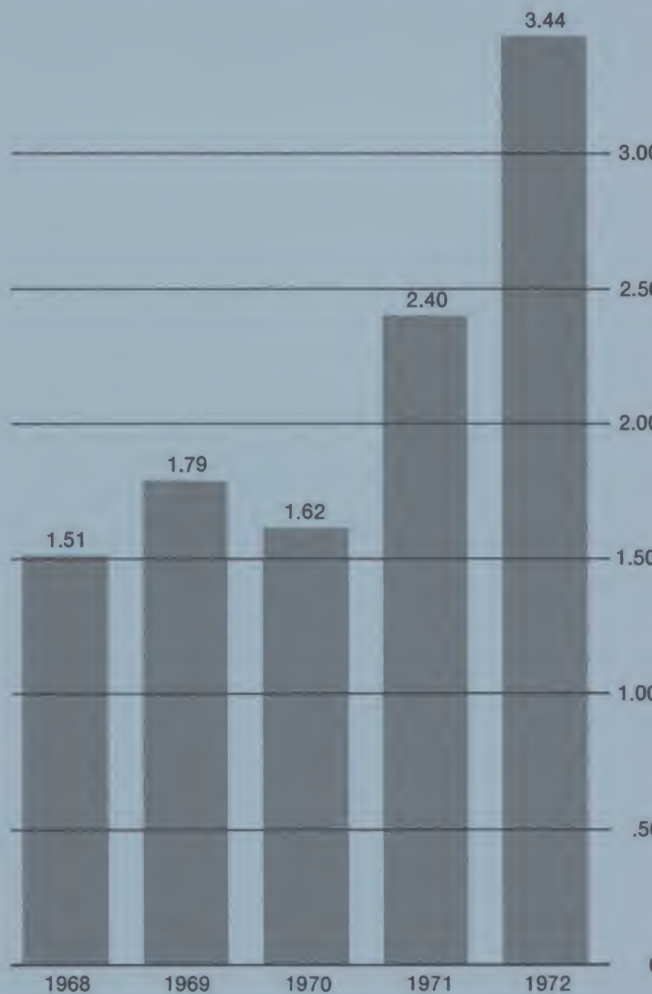
Manufacturing and Merchandising:
net sales and revenues in thousands of dollars

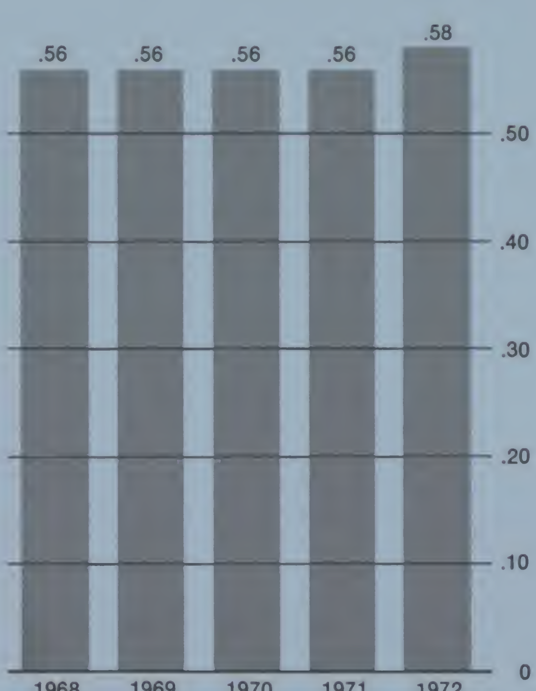


Net income in thousands of dollars



Net income per common share in dollars





Cash dividend per common share
in dollars

D. H. Baldwin Company and Subsidiaries

Consolidated Balance Sheet
December 31, 1972, with comparative figures for 1971

Assets	**1972**	**1971**
Cash and due from banks, including certificates of deposit of $16,400,000 ($7,500,000 in 1971)	**$ 95,649,218**	$ 72,467,821
Investment securities (notes 3, 5, and 8):		
U.S. government and agencies securities	**37,581,464**	32,203,631
Obligations of states and political subdivisions, and possessions	**36,525,273**	29,846,435
Public utility and industrial bonds	**22,126,421**	21,312,870
Corporate stocks and other securities	**21,185,653**	14,811,139
Total investment securities	**117,418,811**	98,174,075
Loans and other receivables (notes 5 and 8):		
Mortgage loans	**307,612,274**	251,885,784
Commercial and industrial loans	**67,192,000**	62,798,000
Consumer and other loans	**170,977,673**	130,247,159
Other	**6,980,641**	8,269,911
	552,762,588	453,200,854
Less: Unearned interest	**17,592,020**	13,394,405
Allowance for losses	**2,310,990**	2,648,431
Net loans and other receivables	**532,859,578**	437,158,018
Federal funds sold and securities purchased under agreements to resell	**22,850,000**	9,618,151
Investments, at underlying net asset value, in manufacturing and merchandising operations (notes 2 and 8):	**20,357,058**	21,504,829
Property and equipment, at cost (note 4):		
Land	**3,563,952**	3,543,013
Buildings and improvements	**10,384,727**	8,294,927
Furniture, fixtures and other equipment	**4,314,969**	4,200,559
	18,263,648	16,038,499
Less accumulated depreciation	**6,496,648**	6,713,542
Net property and equipment	**11,767,000**	9,324,957
Excess of cost of consolidated subsidiaries over the company's share of the fair value of net underlying assets at date of acquisition (note 6)	**21,767,985**	22,928,460
Unamortized insurance acquisition costs	**9,221,482**	8,337,614
Other assets (note 4)	**9,595,762**	9,106,451
	$841,486,894	$688,620,376

See accompanying notes to consolidated financial statements.

Liabilities and Stockholders' Equity	1972	1971
Time and savings deposits	**$399,792,311**	$314,858,310
Demand deposits (note 3)	**164,550,008**	133,726,298
Notes and mortgages payable (note 4):		
Due in one year	**21,949,997**	17,792,083
Due after one year	**44,648,224**	38,724,946
	66,598,221	56,517,029
Federal funds purchased and securities sold under agreements to repurchase	**30,651,881**	21,951,881
Advances from Federal Home Loan Bank (note 5)	**27,987,850**	27,987,850
Insurance reserves	**44,293,391**	39,983,992
Loans in process	**16,599,608**	11,719,170
Advances by borrowers for taxes and insurance	**8,726,239**	7,370,937
Accounts payable and other liabilities	**15,441,560**	14,042,911
Taxes on income, of which $2,755,918 is deferred ($4,046,377 for 1971) (note 6)	**2,874,252**	4,296,377
Deferred income	**787,662**	1,579,609
	778,302,983	634,034,364
Minority interest in subsidiaries	**1,789,454**	1,302,920
Stockholders' equity (notes 4, 7 and 9):		
Preferred stock:		
Series A 5% cumulative convertible, par value $108 per share. Authorized 76,046.5 shares; issued 61,383 shares (66,867 shares in 1971)	**6,629,335**	7,221,655
Series B 8% cumulative, par value $100 per share. Authorized 144,138 shares; issued 71,327 shares (71,079 shares in 1971)	**7,132,662**	7,107,927
Common stock, without par value. Authorized 6,000,000 shares (4,000,000 shares in 1971), issued 2,635,597 shares at stated value (2,465,942 shares in 1971)	**5,271,194**	4,931,884
Additional capital	**8,677,693**	4,041,772
Retained earnings (including appropriated reserves of savings and loan services of $2,374,327 and $1,683,476, respectively)	**34,099,427**	30,329,370
	61,810,311	53,632,608
Less cost of treasury shares:		
Common, 15,260 shares (13,915 shares in 1971)	**285,636**	247,363
Preferred, 1,329 Series B shares (1,021 shares in 1971)	**130,218**	102,153
Total stockholders' equity	**61,394,457**	53,283,092
Commitments and contingencies (note 8)		
	$841,486,894	$688,620,376

D. H. Baldwin Company and Subsidiaries

Consolidated Statement of Income
Year ended December 31, 1972, with comparative figures for 1971

	1972	1971
Banking and other financial services:		
Interest and fees on loans	**$22,332,697**	$18,275,012
Income on investments	**2,649,259**	2,615,721
Other revenues, including security gains of $743,518 ($871,445 in 1971)	**3,630,221**	4,267,400
	28,612,177	25,158,133
Expenses:		
Interest	**8,590,888**	8,199,779
Provision for loan losses	**1,769,165**	1,530,448
Operating expenses	**11,243,130**	9,993,617
Federal income taxes (note 6)	**2,007,962**	1,963,356
	23,611,145	21,687,200
Income from banking and other financial services*	**5,001,032**	3,470,933
Savings and loan services:		
Interest and fees on loans	**21,755,945**	17,221,484
Income on investments	**1,108,920**	816,475
Other revenues, including sale of developed real estate	**869,206**	2,177,917
Equity increase in Anchor Savings Association	**593,505**	—
	24,327,576	20,215,876
Expenses:		
Interest	**13,728,362**	11,430,657
Operating expenses	**3,688,148**	2,823,845
Cost of developed real estate sold	**390,371**	1,653,647
Federal income taxes (note 6)	**1,601,594**	864,018
	19,408,475	16,772,167
Income from savings and loan services (including appropriated to reserves of $690,851 and $713,430)*	**4,919,101**	3,443,709
Insurance services:		
Life and health premiums	**10,824,119**	9,771,466
Property and casualty premiums	**24,187,271**	21,883,633
Investment income, net of expenses of $444,679 ($263,444 in 1971)	**3,406,524**	3,346,664
Security gains	**215,328**	290,756
	38,633,242	35,292,519
Expenses:		
Life and health insurance benefits	**7,072,279**	6,389,892
Property and casualty insurance and adjustment expenses	**15,723,586**	14,257,607
Commissions and brokerage incurred	**3,717,601**	3,679,546
Operating and administrative expenses	**8,347,466**	7,642,256
Federal income taxes (note 6)	**1,247,408**	1,230,984
	36,108,340	33,200,285
Income from insurance services (including income from life insurance operations of $1,599,121 and $1,065,098)*	**2,524,902**	2,092,234
Equity increase in manufacturing and merchandising operations (note 2)*	**839,156**	1,194,918
Unallocated holding company expenses, net of Federal income tax credit of $3,210,000 and $2,873,000:		
Interest	**2,568,699**	2,369,022
Administration	**909,095**	785,980
	3,477,794	3,155,002
Net income	**$ 9,806,397**	$ 7,046,792
Primary income per common share	**$3.44**	$2.40
Fully diluted income per share	**$3.19**	$2.26

*Does not include unallocated holding company interest and administration expenses, net of related Federal income tax credit.

See accompanying notes to consolidated financial statements.

D. H. Baldwin Company and Subsidiaries

Consolidated Statement of Stockholders' Equity
Year ended December 31, 1972, with comparative figures for 1971

	1972	1971
Preferred stock:		
Series A:		
Beginning of year	**$ 7,221,655**	$ 7,305,795
Conversion of 5,255 shares (779 in 1971) to 24,307 common shares (3,467 in 1971)	**(567,585)**	(84,140)
Conversion of 229 shares to 247 shares of Series B	**(24,735)**	—
End of year	**6,629,335**	7,221,655
Series B:		
Beginning of year	**7,107,927**	7,107,927
Conversion of 229 shares of Series A to 247 shares	**24,735**	—
End of year	**7,132,662**	7,107,927
Common stock:		
Beginning of year	**4,931,884**	4,714,584
Issuance of 100,449 shares (94,348 in 1971) as a 4% common stock dividend	**200,898**	188,696
Issuance of 44,899 shares (10,835 in 1971) under employee stock purchase and stock option plans (note 7)	**89,798**	21,670
Conversion of 5,255 shares (779 in 1971) of Series A to 24,307 shares (3,467 in 1971)	**48,614**	6,934
End of year	**5,271,194**	4,931,884
Additional capital:		
Beginning of year	**4,041,772**	1,546,353
Increase applicable to:		
Common shares issued under employee stock purchase and stock option plans	**714,583**	153,718
Conversion of Series A shares to common shares	**518,741**	77,139
4% common stock dividend	**3,390,177**	2,264,352
Transactions in treasury shares	**12,420**	210
End of year	**8,677,693**	4,041,772
Retained earnings:		
Beginning of year	**30,329,370**	28,086,103
Net income	**9,806,397**	7,046,792
Cash dividends:		
Preferred stock, Series A — $5.40 per share and Series B — $8.00	**(910,246)**	(924,302)
Common stock — $.58 ($.56 in 1971) per share, after adjustment for 4% stock dividends in 1972 and 1971 plus fractional shares on stock dividend of $39,712 ($13,687 in 1971) paid in cash	**(1,535,042)**	(1,426,175)
4% common stock dividend	**(3,591,052)**	(2,453,048)
End of year	**34,099,427**	30,329,370
Less common treasury shares:		
Beginning of year	**247,363**	182,127
Purchase of 1,591 shares (3,072 in 1971) less sales of 832 shares (20 in 1971)	**38,273**	65,236
End of year	**285,636**	247,363
Less preferred, Series B treasury shares:		
Beginning of year	**102,153**	98,642
Purchase of 308 shares (35 in 1971)	**28,065**	3,511
End of year	**130,218**	102,153
Total stockholders' equity	**$61,394,457**	$53,283,092

See accompanying notes to consolidated financial statements.

D. H. Baldwin Company and Subsidiaries

Consolidated Statement of Changes in Financial Position
Year ended December 31, 1972, with comparative figures for 1971

	1972	1971
Source of funds:		
Operations:		
Consolidated net income	**$ 9,806,397**	$ 7,046,792
Add (deduct) items not requiring or providing funds in the current period:		
Increase in insurance reserves	**4,309,399**	4,133,981
Increase in unamortized insurance acquisition costs	**(883,868)**	(924,831)
Provision for losses on loans and other receivables	**2,119,410**	1,870,377
Equity increases in manufacturing and merchandising operations and other investments	**(1,432,659)**	(1,194,918)
Provision for deferred Federal income taxes (note 6)	**1,687,543**	2,821,826
Depreciation	**618,873**	678,657
Other	**(356,604)**	504,046
Funds provided from operations	**15,868,491**	14,935,930
Increase in time, savings and demand deposits	**115,757,711**	63,690,921
Federal funds and other money market obligations, net	**—**	12,033,730
Proceeds from issuance of long-term debt	**24,000,000**	3,200,000
Increase in short-term debt	**8,273,000**	—
Proceeds from sales of installment receivables	**5,065,959**	15,200,488
Increase in unearned interest	**4,197,615**	3,671,338
Increase in accounts payable and other liabilities	**1,398,649**	1,996,468
Increase in advances by borrowers for taxes and insurance	**1,355,300**	1,143,475
Proceeds from issuance of common stock under employee stock purchase and stock option plans	**804,381**	175,388
Payments from manufacturing and merchandising operations	**1,826,139**	4,115,065
	178,547,245	120,162,803
Use of funds:		
Cash dividends	**2,445,288**	2,350,477
Increase in loans and other receivables before proceeds from sales of installment receivables	**102,204,106**	76,216,212
Increase in investment securities	**18,439,252**	15,027,435
Decrease in short-term debt	**—**	702,721
Payments on long-term debt	**22,191,808**	12,646,779
Decreases in advance from Federal Home Loan Bank of Topeka	**—**	8,250,000
Federal funds and other money market obligations, net	**4,531,849**	—
Decrease in taxes on income	**1,949,193**	880,832
Purchases of property and equipment, net	**3,060,916**	524,881
Other	**543,436**	1,062,578
	155,365,848	117,661,915
Increase in cash	**23,181,397**	2,500,888
Consolidated cash balances at beginning of year	**72,467,821**	69,966,933
Consolidated cash balances at end of year	**$ 95,649,218**	$ 72,467,821

See accompanying notes to consolidated financial statements.

D. H. Baldwin Company and Subsidiaries

Notes to Consolidated Financial Statements
December 31, 1972

1) Accounting Principles

A) Consolidation policy

Effective December 31, 1972, as part of a plan to restructure the internal organizational structure of the D. H. Baldwin Company (Company), the Company was merged with its subsidiary which was engaged exclusively in the sale and financing of keyboard and other musical instruments and related accessories manufactured by or for the Company. In connection with such plan, a captive finance subsidiary, Baldwin Finance Company (BFC), was organized into which were contributed the assets and related liabilities applicable to the Company's installment financing operation. Further, another subsidiary was formed called Baldwin Piano & Organ Company (BP & O) into which were contributed the assets and related liabilities applicable to the manufacturing and sales operations of musical instruments. As a result of the plan, the Company became principally a holding company as of December 31, 1972.

The accompanying consolidated financial statements include the accounts of the Company and all of its subsidiaries engaged in financial services activities including BFC, Baldwin-Central, Inc. (BCI) and its subsidiaries: The Central Bank and Trust Company (Central Bank), The Empire Savings, Building and Loan Association (Empire), and National Farmers Union Service Corporation (NFU) and their subsidiaries; and certain other subsidiaries. Manufacturing and merchandising operations (music and electronics) of the Company and its subsidiaries engaged in manufacturing and merchandising operations are reported on a one-line equity basis. Corporate interest and general office expenses incurred by the Company, less the related Federal income tax benefit, have not been allocated to the various product lines in the accompanying consolidated statement of income as it is the Company's policy to allocate only income and expense items that can be directly identified with such product lines.

In the prior year, the consolidated financial statements included all operations including manufacturing and merchandising, and allocated corporate interest and general office expenses by product line. The consolidated financial statements for the year ended December 31, 1971, included herein for comparative purposes have been reclassified from amounts previously reported to consolidated operations on the same basis as the current year, and to reflect retroactively the new organizational structure.

All material intercompany transactions and balances have been eliminated.

BCI's investment in NFU, an insurance holding company, is represented by 4% convertible, participating, cumulative preferred stock having a par value of $14,750,000. The preferred stock may be converted into 90% of the outstanding common stock of NFU at BCI's option until January 1, 1975, at which date conversion into common stock is mandatory. In view of this provision and other related agreements, NFU is considered a subsidiary for accounting purposes.

The consolidated financial statements include the accounts of Central Bank, Empire, and NFU after adjustment for purchase price accounting applied as of the dates of acquisition. In addition, consistent with the prior year, the accounts of the insurance companies owned by NFU have been included on the basis of generally accepted accounting principles, which accounting principles differ in some respects from those followed in reports to regulatory authorities.

B) Investment securities

Government and corporate bonds owned by Central Bank and NFU aggregating $102,641,959 ($81,309,522 at December 31, 1971) are stated at cost adjusted for amortization of premiums and accretion of discounts over the terms of the securities. All other investment securities are stated at cost except for the Company's investments in Siliconix incorporated and Anchor Savings Association, aggregating $4,806,946 ($4,022,340 at December 31, 1971) which are carried at cost plus the Company's share of equity increases since dates of acquisition.

Gains and losses are recognized when securities are sold as the difference between net sales proceeds and adjusted cost.

The total market value of investment securities exceeds cost.

C) Loans and other receivables

Consumer loans made by Central Bank are recorded at the amount disbursed plus the interest to be earned over the term of the loan. The interest is recorded as "unearned interest" and amortized to operating income using the rule of the 78ths method.

Consumer and other loans include $16,217,953 ($7,732,637 at December 31, 1971) of installment contracts arising from the sale of musical instruments which are accepted from customers, with recourse to the musical instrument dealers. Finance charges from such installment loans are taken into income on the straight-line basis as cash is received from the customer.

Loan origination fees received by Empire are deferred for amounts in excess of 1% of the loan plus $100 for nonconstruction loans and 2% of the loan plus $100 for construction loans. In accordance with the change in regulations for insurance of accounts, in 1972, Empire changed from the straight-line to the sum-of-the-months digits method of amortizing deferred loan fees into income over seven years for loans originated prior to January 1, 1972, and ten years for loans originated thereafter. The new method was adopted to better relate fee income to unpaid loan principal balances and has been applied retroactively to deferred loan fees of prior years. The effect of the change on 1972 income was insignificant. The adjustment, $341,728, to apply the new method retroactively is included in income for 1972. The pro forma net income for the savings and loan product line and for the total net income for the Company for 1971 assuming the new amortization method was applied retroactively are $3,530,977 and $7,134,060, respectively.

D) Allowance for losses

It is the policy for Central Bank to provide for loan losses through a charge to operations based on a historical five year moving average of net loan losses to outstanding loans.

BFC provides an allowance for doubtful accounts through a charge to operations based on a percentage of new business. Such allowance, as are allowances for losses on all remaining receivables, is adjusted for such other factors which, in management's judgment, deserve recognition in estimating possible loan losses.

Except for Empire, loans and other receivables deemed to be uncollectible are charged to allowance for losses.

Empire's policy for financial statement purposes is to charge operations for estimated losses on specific loans where any significant and permanent decline reduces the market value of the underlying security to less than the loan. Such losses are usually indicated during foreclosure proceedings.

E) Property and equipment

Depreciation of property and equipment is accumulated on the straight line and accelerated methods over the estimated useful lives of the related property. The estimated useful lives are principally as follows:

Description	Years
Buildings	25 - 60
Building improvements	10 - 40
Furniture, fixtures and other equipment	4 - 15

The accounting policy is to charge maintenance, repairs and minor renewals and betterments of property and equipment to expense in the year incurred. Major expenditures for renewals and betterments are capitalized and depreciated or amortized over their estimated useful lives. On disposal or retirement, the related cost and accumulated depreciation are eliminated from the accounts and gain or loss on the transaction is reflected in the consolidated statement of income.

F) Intangibles

The amount by which the Company's cost of certain subsidiaries acquired prior to October 30, 1970, exceeds its share of the fair value of the net assets of such subsidiaries at the dates of acquisition is not being amortized because, in the opinion of management, its value has not diminished.

G) Unamortized insurance acquisition costs, insurance reserves, and insurance revenue and expenses

Recognition of Premium Revenue and Related Expenses:

Premiums on life insurance contracts are generally recognized as revenue when due, which is reasonably in proportion to performance under such contracts. Premiums on accident and health contracts and on property and casualty insurance contracts are taken into earnings over the periods covered by the policies. Benefits and expenses on insurance contracts are associated with earned premiums so as to result in recognition of profits over the lives of the contracts. This association is accomplished by means of the provisions for future policy benefits, claims and losses, and the amortization of acquisition costs.

Deferred Insurance Acquisition Costs:

The costs of acquiring new business, principally commissions, certain expenses of the policy issuance and underwriting department and certain variable agency expenses, all of which vary with and are primarily related to the production of new business, have been deferred. These deferred acquisition costs are being amortized over periods benefited while the policies are in force.

Policy Liabilities:

Liabilities for future policy benefits on life insurance have been computed by a net level premium method based upon future investment yield, mortality and withdrawals.

Liabilities for unpaid claims, losses and loss adjustment expenses are based upon accumulated case estimates for losses reported prior to the close of the period and estimates of unreported losses and loss adjustment expenses based on past experience, reduced by estimated amounts recoverable through reinsurance.

Property and casualty insurance unearned premiums are determined on a monthly pro-rata basis and represent that portion of premiums written which are applicable to the unexpired terms of policies in force, reduced by respective reinsurance premiums.

H) Income Taxes

Deferred Federal income taxes have been provided for income and expenses which enter into the determination of pre-tax accounting income and taxable income in different periods. Such timing differences consist principally of Central Bank's use of the cash method of accounting for Federal income tax purposes, Empire's different basis of reporting loan fee income and interest earned on prepayments to the Federal Savings and Loan Insurance Corporation secondary reserve, and benefits on prepaid acquisition costs associated with unearned premiums on casualty insurance business and on deferred costs of acquiring life insurance business. Acquisition costs are deductible in the year incurred for income tax purposes.

Investment tax credits, which are not material, have been accounted for on the "flow-through" method, which recognizes the benefit in the year in which the assets giving rise to the credit are placed in service.

In accordance with the provisions of the Internal Revenue Code, Empire has appropriated for specific tax bad debt reserves approximately $13,800,000 through December 31, 1972 (of which $5,887,000, including a current appropriation of approximately $2,400,000, has been appropriated since its acquisition by BCI in 1968) as a deduction from taxable income for which, in accordance with generally accepted accounting principles, deferred income taxes have not been provided. If, in the future, these reserves are charged for any purpose other than to absorb bad debt losses, a tax liability will be imposed upon Empire at the then current Federal income tax rate.

The life insurance subsidiary of NFU is subject to taxation under the provisions of the Life Insurance Income Tax Act of 1959 which provides generally that one-half of the excess, if any, of gains from operations over taxable investment income, less certain special deductions is taxable to the life insurance company only when distributed to stockholders as dividends. Such accumulated amount is estimated at $1,836,000 as of December 31, 1972. If, in the future, the income is distributed to stockholders, a tax liability will be imposed upon NFU at the then current Federal income tax rate.

I) Appropriated reserves of Savings and Loan Services

The appropriated reserves (retained earnings) have been established in accordance with rules and regulations of supervisory authority solely for the purpose of absorbing future losses, if any.

J) Retirement Plans

The Company and its subsidiaries maintain various contributory and non-contributory pension plans covering all eligible employees. The companies accrue all actuarially determined costs. Past service costs are being amortized over periods ranging from 25 to 40 years. The policy is to fund pension costs. Under certain plans, the Company has chosen to fund the minimum contribution requirements as actuarially determined under the plans. Total pension expense, including amounts charged to manufacturing and merchandising operations, amounted to $741,000 ($620,500 in 1971).

K) Net Income Per Share

Primary income per common share has been computed based on the weighted average number of shares outstanding during the year, after consideration of preferred dividend requirements, a two for one stock split on June 21, 1971 and the 4% stock dividends in 1972 and 1971. Fully diluted income per share has been computed assuming conversion of the Series A preferred stock and elimination of the dividend requirement thereon.

December 31, 1971:	Financial Services: Banking and Other Financial Services	Savings and Loan Services	Insurance Services
Assets:			
Cash and due from banks	$ 58,671,424	$ 9,101,884	$ 774,574
Investment securities	49,832,063	11,195,762	35,025,563
Loans and other receivables	199,434,782	225,749,678	9,789,420
Federal funds sold and securities purchased under agreements to resell	9,618,151	—	—
Property and equipment, at cost less depreciation	3,752,537	4,122,493	568,581
Excess of cost of consolidated subsidiaries over the company's share of the fair value of net underlying assets at dates of acquisition	6,786,119	9,127,527	7,014,814
Unamortized insurance acquisition costs	—	—	8,337,614
Other	5,462,529	1,647,357	1,619,156
Total assets	333,557,605	260,944,701	63,129,722
Liabilities:			
Time, savings and demand deposits	260,437,298	188,147,310	—
Notes and mortgages payable	5,990,498	—	3,887,531
Other borrowings	21,951,881	27,987,850	—
Insurance reserves	—	—	39,983,992
Loans in process	—	11,719,170	—
Advances by borrowers for taxes and insurance	—	7,370,937	—
Other liabilities	8,527,904	1,357,756	4,614,188
Minority interest	—	—	1,302,920
Deferred income	54,613	1,524,996	—
Total liabilities	296,962,194	238,108,019	49,788,631
Net assets	$ 36,595,411	$ 22,836,682	$13,341,091

In connection with the acquisition of Empire, the Company agreed with regulatory authorities that until November, 1973, Empire will not declare dividends whenever dividend payments would reduce Empire's net worth below 8% of certain assets. At December 31, 1972, the net worth of Empire was approximately 7.6% of such assets; however, Empire could have satisfied this 8% requirement through the sale of mortgage loans and repayment of debt of approximately $10,000,000.

Under provisions of the 5¼% subordinated capital debenture issued by Central Bank (see note 4), there are certain restrictions on the payment of cash dividends. At December 31, 1972, $4,224,240 was available for cash dividends under the terms of the agreement. Central Bank declared cash dividends aggregating $1,758,000 in 1972 and $1,224,000 in 1971.

A summary balance sheet of D. H. Baldwin Company at December 31, 1972, carrying its investments in financial services subsidiaries and investments in the manufacturing and merchandising operations on a one-line equity basis, and a summary of changes in financial position for the year then ended after adjustments for the internal reorganization as described in note (1)(A) are as follows:

Summary Balance Sheet, December 31, 1972

Assets		
Current assets:		
Cash		$ 962,183
Sundry receivables		1,006,090
Prepaid expense		130,797
Total current assets		2,099,070
Property and equipment, less accumulated depreciation of $2,354,853		980,197
Investments and advances:		
Financial services subsidiaries, including advances of $4,067,325	$85,571,746	
Manufacturing and merchandising operations including advances of $1,787,350	20,357,058	
Other investments, at cost plus equity increases	5,077,802	111,006,606
Deferred charges and other assets		792,906
		$114,878,779
Liabilities and Stockholders' Equity		
Current liabilities:		
Notes payable to banks and other		6,585,000
Long-term debt, current portion		1,846,000
Accounts payable and accrued expenses		1,369,407
Taxes on income		115,000
Total current liabilities		9,915,407
Long-term debt, less current portion		43,024,000
Other liabilities		335,500
Deferred Federal income taxes		209,415
Stockholders' equity		61,394,457
		$114,878,779

Summary of Changes in Financial Position, Year Ended December 31, 1972

Source of funds:	
Operations:	
Net income	$ 9,806,397
Add (deduct) items not requiring or providing funds in the current period:	
Equity increases in investments	(12,648,774)
Depreciation	175,267
Provision for deferred Federal income taxes	413,700
Funds used in operations	(2,253,410)
Proceeds from issuance of long-term debt	24,000,000
Dividends declared by financial service subsidiaries	1,806,495
Payments from subsidiaries, net	1,931,451
Issuance of common stock	804,381
	$ 26,288,917
Use of funds:	
Cash dividends	2,445,288
Payments on long-term debt, less change in current portion	17,546,000
Decrease in deferred Federal income taxes	2,059,990
Increases in property and equipment, net	274,118
Other, net	783,332
Increase in working capital	3,180,189
	$ 26,288,917
Changes in working capital:	
Decrease in current assets	4,370,812
Decrease in current liabilities	7,551,001
	$ 3,180,189

2) Supplemental financial information

A condensed summary of the net assets employed in the consolidated product lines at December 31, 1972 and 1971 are as follows:

	Financial Services		
December 31, 1972:	Banking and Other Financial Services	Savings and Loan Services	Insurance Services
Assets:			
Cash and due from banks	$ 76,891,803	$ 16,745,872	$ 1,049,360
Investment securities	67,998,702	6,411,179	40,795,483
Loans and other receivables	242,740,810	279,432,709	9,679,969
Federal funds sold and securities purchased under agreements to resell	22,850,000	—	—
Property and equipment, at cost less depreciation	6,013,285	4,196,727	576,791
Excess of cost of consolidated subsidiaries over the company's share of the fair value of net underlying assets at dates of acquisition	6,825,343	9,127,527	5,815,115
Unamortized insurance acquisition costs	—	—	9,221,482
Other	5,738,510	1,339,941	1,593,606
Total assets	429,058,453	317,253,955	68,731,806
Liabilities:			
Time, savings and demand deposits	330,204,861	234,137,458	—
Notes and mortgages payable	18,949,114	—	1,924,107
Other borrowings	30,651,881	27,987,850	—
Insurance reserves	—	—	44,293,391
Loans in process	—	16,599,608	—
Advances by borrowers for taxes and insurance	—	8,726,239	—
Other liabilities	10,419,201	1,028,700	4,838,588
Minority interest	—	—	1,789,454
Deferred income	5,741	781,921	—
Total liabilities	390,230,798	289,261,776	52,845,540
Net assets	$ 38,827,655	$ 27,992,179	$15,886,266

Condensed Statement of Net Assets employed in the manufacturing and merchandising operations as of December 31, 1972 and Condensed Income Statement for the years ended December 31, 1972 and 1971 are as follows:

Condensed Statement of Net Assets Employed
December 31, 1972

Assets	
Current assets:	
Cash	$ 390,016
Accounts receivable, net of allowance for losses of $865,904	7,380,784
Inventories at the lower of cost (first-in, first-out) or market	17,240,593
Prepaid expenses and deposits	596,067
Total current assets	25,607,460
Property, plant and equipment, net of accumulated depreciation of $5,305,559	5,362,742
Investment in Siliconix incorporated, at cost plus equity increases	1,912,276
Intangibles and other assets	392,670
	$ 33,275,148
Liabilities	
Current liabilities:	
Notes payable, bank	425,000
Accounts payable	1,239,861
Accrued expenses	4,164,913
Total current liabilities	5,829,774
Other liabilities	676,040
Deferred Federal income taxes	4,500,000
Net assets employed	22,269,334
	$ 33,275,148
Consists of:	
Investments at underlying net asset value in manufacturing and merchandising operations	20,357,058
Investment in Siliconix incorporated	1,912,276
	$ 22,269,334

Condensed Income Statement
Years Ended December 31, 1972 and 1971

	1972	1971
Net sales	**$ 63,332,881**	$ 52,154,722
Cost of goods sold	**47,218,205**	36,471,348
Gross profit on sales	**16,114,676**	15,683,374
Equity increase in Siliconix incorporated	**160,786**	70,994
Other revenues	**410,820**	597,498
Gross profit	**16,686,282**	16,351,866
Selling, general and administrative expenses, including depreciation of $839,717 and $739,445	**15,447,126**	14,165,948
Net income before Federal income taxes	**1,239,156**	2,185,918
Federal income taxes	**400,000**	991,000
Net income	**$ 839,156**	$ 1,194,918
Net income (loss) allocated to:		
Music	**1,320,034**	1,347,947
Electronics	**(480,878)**	(153,029)
	$ 839,156	$ 1,194,918

Musical instruments in the amount of approximately $12,903,000 have been sold to the D. H. Baldwin Trust. At December 31, 1972, the Trust had issued notes payable to banks of $12,300,000. The Trust has shipped these instruments on consignment to Baldwin musical instrument dealers.

3) Investment Securities

The approximate amortized cost of investment securities pledged by Central Bank to secure public funds on deposit amounted to $36,310,000 and $22,180,000, at December 31, 1972 and 1971, respectively.

4) Notes and mortgages payable (short and long-term)

	December 31 1972	December 31 1971
Banks:		
Note payable dated December 29, 1972, bearing interest at 110% of the bank's prime rate (at December 31, 1972 the effective rate was 6.6%), payable in installments of $625,000 semi-annually 1975 through 1978, and $1,250,000 semi-annually 1979 and 1980	**$10,000,000**	$ —
Note payable dated December 13, 1972, bearing interest at 1% above the six month rate at which United States dollars are offered to prime banks in the London Interbank Market (at January 12, 1973, the effective rate was 7¼%), payable in installments of $125,000 semi-annually 1975 through 1978, and $250,000 semi-annually 1979 and 1980	**2,000,000**	—
Note payable bearing an 8⅜% interest rate with principal payable $1,000,000 annually 1973 through 1975, and a final payment of $2,000,000 due in 1976	**5,000,000**	5,000,000
Notes payable bearing a variable interest rate of 1½% above the six month rate at which United States dollars are offered to prime banks in the London Interbank Market, due 1974 through 1977 (paid in full in 1972)	**—**	10,000,000
Notes payable bearing a variable interest rate of 1% above the average interest rates at which the participating banks' London offices are able to acquire six months United States dollars, due June 30, 1972 through June 30, 1974 (paid in full in 1972)	**—**	5,000,000
Notes payable bearing interest at 1% above the prime rate and 6%, secured by the common stock of the life insurance subsidiary of NFU in 1972 and 1971, and pledge of bonds in the principal amount of $1,800,000 in 1971; $1,800,000 due in 1972 and $1,400,000 due in 1974	**1,400,000**	3,200,000
Note payable — interest at 6½%, paid in 1972	**—**	523,082
Short-term notes bearing interest of 5¾% to 6% at December 31, 1972, due currently	**15,235,000**	260,000
	33,635,000	23,983,082
Other:		
8½% notes dated December 1, 1972, due December 1, 1992, $670,000 payable annually 1979 through 1991, with the balance due 1992	**12,000,000**	—
Note payable bearing an interest rate of 8% with principal amounts payable in varying amounts through April 1, 1992, of which $846,000 is due in 1973	**10,870,000**	11,650,000
Note payable bearing an interest rate of 5%, payments due annually through 1975, paid in full in 1972	**—**	3,600,000
Commercial paper bearing interest of 5¼% to 6% at December 31, 1972	**4,427,000**	11,129,000
5¼% subordinated capital debenture, payable $200,000 annually	**2,400,000**	2,600,000
	29,697,000	28,979,000
Mortgages payable, due in monthly installments aggregating $34,728 including interest, at annual rates of 4⅝% to 6% with maturities ranging from May, 1979 to March, 1988, secured by land, buildings and improvements with an approximate carrying value of $3,226,000 and investment in real estate of approximately $2,704,000	**3,266,221**	3,554,947
	$66,598,221	$56,517,029

The approximate maturities of notes and mortgages payable for the next five years ended after December 31, 1973 are as follows:

1974	$3,505,000
1975	3,704,000
1976	4,359,000
1977	3,070,000
1978	2,898,000

The notes dated December 1, 13, and 29, 1972, contain certain restrictions as to the creation of liens, new indebtedness, leases, and investments, and have limitations as to the payment of dividends in cash or other property and retirement of capital stock. Under the most restrictive covenants, 75% of the net income of the Company earned after December 31, 1972, will be available for payment of dividends or retirement of capital stock, subject to the net worth of certain subsidiaries meeting certain defined tests.

5) Advances from Federal Home Loan Bank

As is the common practice in the savings and loan industry, first mortgage real estate loans totalling approximately $40,137,000 ($45,793,000 at December 31, 1971) and stock of the Federal Home Loan Bank of Topeka, Kansas, totalling $3,027,300, included in investment securities, were pledged by Empire as collateral for advances from the Federal Home Loan Bank totalling $27,987,850 at December 31, 1972 and 1971.

The advances bear interest at from 6¼% to 8.10% and mature on various dates through 1976.

The maturities by year are as follows:

1973	$ 8,470,444
1974	9,458,703
1976	10,058,703
	$27,987,850

6) Income Taxes

The income tax provision includes a deferred provision of $1,687,543 and $2,821,826, respectively, for the years ended December 31, 1972 and 1971 arising principally from the timing differences described in note (1)(H). The provision for income taxes has been reduced due to income on tax-exempt bonds held by Central Bank which is not taxable for Federal income tax purposes.

Income taxes for 1972 reflect the tax benefit, $370,000, arising from the sale of investment securities which had a higher tax basis than the proceeds received from sale. For accounting purposes, the Company recorded a gain on such sale of approximately $426,000 for which no taxes are required. Such securities were acquired in 1969 in connection with the Bowfund Corporation merger.

As a result of the adjustments for purchase price accounting as explained in note (1)(A) income includes $205,951, $972,583 and $745,435 from banking, savings and loan, and insurance services which represent permanent differences and, therefore, no income taxes have been provided since such amounts were tax effected at dates of acquisition.

In addition, NFU's life insurance subsidiary includes income of $576,725 which is applicable to deferred life insurance acquisition costs affecting only gain from operations which will have no tax effect when it reverses. Therefore, no income taxes have been provided on this excess.

The Company files consolidated Federal income tax returns with all its subsidiaries except NFU. NFU files a consolidated Federal income tax return with its eligible subsidiaries, and its life insurance subsidiary files a separate return. NFU utilized operating loss carryovers from 1968 to offset taxable income of $2,776,000 and $1,417,159 in 1972 and 1971, respectively. The benefit from the operating loss carryovers of $1,199,700 and $637,200, respectively, have been credited to Excess of cost of consolidated subsidiaries over the company's share of the fair value of the net underlying assets at date of acquisition, as an adjustment of the purchase price accounting applied as of the date of acquisition of NFU.

7) Capital Stock

On May 21, 1971 (effective June 21, 1971) the Board of Directors approved a two for one split of the common stock and reduced the stated value of each common share from $4.00 to $2.00. All references to number of shares of common stock, and related dividends and income per share give effect to such stock split.

All references to shares of common stock and price per share in this note gives effect to the 4% stock dividends in 1972 and 1971.

At December 31, 1972 and 1971, 295,682 and 322,100 shares, respectively, of common stock were reserved for conversion of the Series A convertible preferred stock, and 85,845 and 132,561 shares, respectively, of common stock were reserved for sale to the Company's employees under the stock purchase plan and for the granting and exercise of options under the stock option plan. Under the stock option plan, options may be granted to certain employees to purchase common stock of the Company at a price not less than the market value on the date of the grant. All outstanding options at December 31, 1972 were exercisable. Stock options granted and exercised during 1972 and 1971 and outstanding at December 31, 1972 are as follows:

	Shares	Option price per share
Options granted		
1972	4,680	$31.13
1971	2,163	14.96
Options exercised		
1972	38,239	$12.02-$15.72
1971	10,816	14.67
Options outstanding at December 31, 1972	36,312	$12.02-$31.13

Each share of the Series A preferred stock is convertible into either 1.08 shares of Series B preferred stock or 4.8 shares of common stock. Each share of preferred stock is entitled to one vote on any matter submitted to a vote of the common shareholders. The preferred stock may be redeemed in whole or in part at the Company's option anytime after July 1, 1989 at par value plus all dividends accrued and unpaid thereon.

In connection with pending bank acquisitions (see note 9), the shareholders will be asked in 1973 to authorize and the Company to register under the Securities Acts 500,000 shares each of two Classes of Preferred stock, having par value of $100, to be known as Class C 4% Cumulative Convertible Preferred Shares, and Class D 8% Cumulative Preferred Shares. Class C shares are to be convertible into common or Class D shares. The new Classes are to be voting, redeemable after 1992, and be subordinate to Series A and B Preferred shares upon liquidation.

8) Commitment and Contingent Liabilities

Following the requirement of the Bank Holding Company Act, the Company filed with the Federal Reserve Board the requisite report to register as a bank holding company. The report and the application of the grandfather clause of the 1970 Amendments to the Bank Holding Company Act to certain non-banking business conducted by the Company are being reviewed by the Federal Reserve Board. The Company has, however, agreed to divest itself of its investments in electronic companies and other investments, all of which aggregate approximately $7,877,000 at December 31, 1972. The aggregate net loss deducted from consolidated net income from these investments amounted to approximately $65,000 for 1972 and $153,000 for 1971.

The Company has sold installment receivable contracts to financial institutions. At December 31, 1972, the total unpaid contract balance of receivables sold amounted to $19,595,000. Under terms of certain of the sales agreements, the Company is obligated to repurchase delinquent accounts up to an amount withheld by the purchasers ($5,470,000 at December 31, 1972). Under the remaining agreements covering accounts sold having aggregate unpaid balances of $8,592,457 at December 31, 1972, the Company must substitute current accounts for any account becoming delinquent. Management is of the opinion that adequate provision has been made in the financial statements for losses arising from the reacquisition of such paper.

Central Bank, through its subsidiary, has entered into a joint venture to participate in the construction and ownership of a new building. Under the terms of the agreement, the Bank and its subsidiary are guarantor for up to $5,500,000 of interim financing during the construction period.

Central Bank has entered into a long-term lease agreement with the joint venture to rent space in the new facility. Under the terms of the lease agreement, the Bank may be responsible for rentals in excess of the amount of rent related to the space it will occupy. Therefore, annual rental payments (beginning February 16, 1973) could range from approximately $625,000 to $975,000. The lease expires in 2008 with provisions to renew for additional periods.

Empire, along with several other Colorado financial institutions, has been named as a defendant in a class action suit demanding that such institutions pay interest on advances by borrowers for taxes and insurance. There is also a pending class action suit which involves revolving credit under credit card contracts. Central Bank participates in such credit. The suits do not provide a basis for determining the amount of any possible liability. Management believes that the suits are not well founded and will not have a material effect on the Company's financial statements.

At December 31, 1972, the Company is obligated under non-cancellable leases for real and personal property expiring on various dates to 2008, including leases by the manufacturing and merchandising operations. Rental expense for 1972 and 1971 under such leases amounts to approximately $687,000 and $584,000, respectively. Minimum rental payments (exclusive of amounts based on sales) for the next five years are approximately $1,226,000 in 1973; $1,186,000 in 1974; $1,174,000 in 1975; $1,007,000 in 1976, and $898,000 in 1977.

9) Pending Acquisitions

The Company has entered into agreements with stockholders or the board of directors has approved letters of intent to acquire ten additional banks in Colorado. The acquisitions will principally require; a) the issuance of Class C 4%, $100 par value, cumulative convertible preferred shares; b) the issuance of common shares in the case of two of the bank acquisitions, the number of which are dependent on market value at date of closing; and c) an agreement to infuse $1,000,000 in additional capital in one bank. The acquisitions are all subject to necessary regulatory approvals, selling shareholder approval and the receipt of a favorable ruling by the Internal Revenue Service, in most cases, and the authorization by Baldwin shareholders and registration under the Securities Acts of two Classes of Preferred shares (see note 7).

Accountants' Report

The Board of Directors and Stockholders
D. H. Baldwin Company:

We have examined the consolidated balance sheet of D. H. Baldwin Company and subsidiaries as of December 31, 1972, and the related statements of income, stockholders' equity and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine the consolidated financial statements of National Farmers Union Service Corporation (a consolidated subsidiary) and its subsidiaries nor the equity increases in certain unconsolidated investments, which statements reflect total assets and net income constituting 8% and 39%, respectively, of the related consolidated totals. These statements were examined by other independent certified public accountants whose reports thereon have been furnished to us and our opinion expressed herein, insofar as it relates to the amounts included for National Farmers Union Service Corporation and subsidiaries and the equity increases in certain unconsolidated investments, is based solely upon the reports of the other auditors.

In our opinion, based upon our examination and the aforementioned reports of other independent certified public accountants, the accompanying consolidated balance sheet and consolidated statements of income, stockholders' equity, and changes in financial position present fairly the financial position of D. H. Baldwin Company and subsidiaries at December 31, 1972, and the results of their operations, the changes in stockholders' equity, and the changes in their financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year after giving retroactive effect to the changes, with which we concur, in the consolidation policy and allocation policy of corporate interest and general office expenses by product line as described in Note 1 to the consolidated financial statements.

Peat, Marwick, Mitchell & Co.

Cincinnati, Ohio
February 23, 1973

D. H. Baldwin Company and Subsidiaries

General Offices: 1801 Gilbert Avenue, Cincinnati, Ohio 45202
Area Code 513/621-4300

Subsidiaries

Financial Services

Baldwin-Central, Inc.
The Central Bank and Trust Company
The Empire Savings, Building and Loan Association
Baldwin Finance Company
The Baldwin Company

Manufacturing and Merchandising

Baldwin Piano & Organ Company
The Baldwin Piano Company (Canada) Limited
Baldwin Export Corporation
C. Bechstein Pianofortefabrik AG
Baldwin Electronics, Inc.
Fabricantes Tecnicos, S.A.

Manufacturing Plants

Arkansas: Booneville, Camden, Conway, DeQueen, Fayetteville, Little Rock
Mississippi: Greenwood
Ohio: Cincinnati
Mexico: Juarez
West Germany: West Berlin, Karlsruhe, Eschelbronn

Investments

National Farmers Union Service Corporation
Siliconix incorporated
Anchor Savings Association

Dealers or Company-Owned Sales Outlets

In all principal cities in the United States, and abroad

Transfer Agents and Registrars

The Central Trust Company, Cincinnati
Transfer Agent and Registrar
Manufacturers Hanover Trust Company, New York
Transfer Agent
First National City Bank, New York
Registrar

Stock Listed

American Stock Exchange (BDW)
Cincinnati Stock Exchange